

**SOUTH CAROLINA STATE AGENCY
OF
VOCATIONAL REHABILITATION
WEST COLUMBIA, SOUTH CAROLINA**

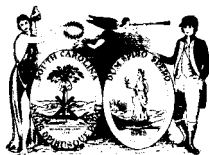
STATE AUDITOR'S REPORT

JUNE 30, 2001

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State of South Carolina



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INDEPENDENT ACCOUNTANT'S REPORT ON APPLYING AGREED-UPON PROCEDURES

October 18, 2002

The Honorable Mark Sanford, Governor
and
Board of Directors
South Carolina State Agency of Vocational Rehabilitation
West Columbia, South Carolina

We have performed the procedures described below, which were agreed to by the governing body and management of the South Carolina State Agency of Vocational Rehabilitation (the State Agency), solely to assist you in evaluating the performance of the State Agency for the fiscal year ended June 30, 2001, in the areas addressed. The State Agency's management is responsible for its financial records, internal controls and compliance with State laws and regulations. This agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of these procedures is solely the responsibility of the specified parties in this report. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

The procedures and the associated findings are as follows:

1. We tested selected recorded receipts to determine if these receipts were properly described and classified in the accounting records and internal controls over the tested receipt transactions were adequate. We also tested selected recorded receipts to determine if these receipts were recorded in the proper fiscal year. We compared amounts recorded in the general ledger and subsidiary ledgers to those in the State's accounting system (STARS) as reflected on the Comptroller General's reports to determine if recorded revenues were in agreement. We made inquiries and performed substantive procedures to determine if revenue collection and retention or remittance were supported by law. We compared current year recorded revenues from sources other than State General Fund appropriations to those of the prior year, and we used estimations and other procedures to determine the reasonableness of collected and recorded amounts by revenue account. We also tested the cooperative agreements the State Agency has with other State agencies to receive funds for a portion or all services provided and verified the services were provided and the correct amounts were collected. The individual transactions selected for testing were chosen randomly. Our finding as a result of these procedures is presented in Timing of Deposits in the Accountant's Comments section of this report.

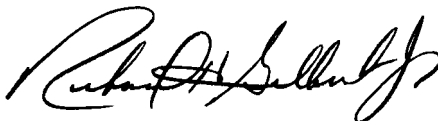
2. We tested selected recorded non-payroll disbursements to determine if these disbursements were properly described and classified in the accounting records, were bona fide disbursements of the State Agency, and were paid in conformity with State laws and regulations; if the acquired goods and/or services were procured in accordance with applicable laws and regulations; and if internal controls over the tested disbursement transactions were adequate. We also tested selected recorded non-payroll disbursements to determine if these disbursements were recorded in the proper fiscal year. We compared amounts recorded in the general ledger and subsidiary ledgers to those in various STARS reports to determine if recorded expenditures were in agreement. We compared current year expenditures to those of the prior year to determine the reasonableness of amounts paid and recorded by expenditure account. The individual transactions selected for testing were chosen randomly. Our finding as a result of these procedures is presented in Reconciliations in the Accountant's Comments section of this report.
3. We tested selected recorded payroll disbursements to determine if the tested payroll transactions were properly described, classified, and distributed in the accounting records; persons on the payroll were bona fide employees; payroll transactions, including employee payroll deductions, were properly authorized and were in accordance with existing legal requirements; and internal controls over the tested payroll transactions were adequate. We tested selected payroll vouchers to determine if the vouchers were properly approved and if the gross payroll agreed to amounts recorded in the general ledger and in STARS. We also tested payroll transactions for selected new employees and those who terminated employment to determine if internal controls over these transactions were adequate. We compared amounts recorded in the general ledger and subsidiary ledgers to those in various STARS reports to determine if recorded payroll and fringe benefit expenditures were in agreement. We performed other procedures such as comparing current year recorded payroll expenditures to those of the prior year; comparing the percentage change in recorded personal service expenditures to the percentage change in employer contributions; and computing the percentage distribution of recorded fringe benefit expenditures by fund source and comparing the computed distribution to the actual distribution of recorded payroll expenditures by fund source to determine if recorded payroll and fringe benefit expenditures were reasonable by expenditure account. The individual transactions selected for testing were chosen randomly. Our finding as a result of these procedures is presented in Workers' and Unemployment Compensation Insurance in the Accountant's Comments section of this report.
4. We tested randomly selected recorded journal entries and operating transfers and all interagency appropriation transfers to determine if these transactions were properly described and classified in the accounting records; they agreed with the supporting documentation, were adequately documented and explained, were properly approved, and were mathematically correct; and the internal controls over these transactions were adequate. We found no exceptions as a result of the procedures.

5. We tested selected entries and monthly totals in the subsidiary records of the State Agency to determine if the amounts were mathematically accurate; the numerical sequences of selected document series were complete; the selected monthly totals were accurately posted to the general ledger; and the internal controls over the tested transactions were adequate. The transactions selected for testing were chosen randomly. We found no exceptions as a result of the procedures.
6. We requested all monthly reconciliations prepared by the State Agency for the year ended June 30, 2001, and tested selected reconciliations of balances in the State Agency's accounting records to those in STARS as reflected on the Comptroller General's reports to determine if they were accurate and complete. For the selected reconciliations, we determined if they were timely performed and properly documented in accordance with State regulations, recalculated the amounts, agreed the applicable amounts to the State Agency's general ledger, agreed the applicable amounts to the STARS reports, determined if reconciling differences were adequately explained and properly resolved, and determined if necessary adjusting entries were made in the State Agency's accounting records and/or in STARS. We judgmentally selected the fiscal month 13 reconciliations for testing. Our finding as a result of these procedures is presented in Reconciliations in the Accountant's Comments section of this report.
7. We tested the State Agency's compliance with all applicable financial provisions of the South Carolina Code of Laws, Appropriation Act, and other laws, rules, and regulations for fiscal year 2001. Our finding as a result of these procedures is presented in Workers' and Unemployment Compensation Insurance in the Accountant's Comments section of this report.
8. We reviewed the status of the deficiencies described in the findings reported in the Accountant's Comments section of the State Auditor's Report on the State Agency resulting from our engagement for the fiscal year ended June 30, 2000, to determine if adequate corrective action has been taken. Our findings as a result of these procedures are presented in Section B in the Accountant's Comments section of this report.
9. We obtained copies of all closing packages as of and for the year ended June 30, 2001, prepared by the State Agency and submitted to the State Comptroller General. We reviewed them to determine if they were prepared in accordance with the Comptroller General's GAAP Closing Procedures Manual requirements; if the amounts were reasonable; and if they agreed with the supporting workpapers and accounting records. Our findings as a result of these procedures are presented in Closing Packages in the Accountant's Comments section of this report.
10. We obtained a copy of the schedule of federal financial assistance for the year ended June 30, 2001, prepared by the State Agency and submitted to the State Auditor. We reviewed it to determine if it was prepared in accordance with the State Auditor's letter of instructions; if the amounts were reasonable; and if they agreed with the supporting workpapers and accounting records. Our findings as a result of these procedures are presented in Closing Packages - Grant/Entitlement Revenues in the Accountant's Comments section of this report.

The Honorable Mark Sanford, Governor
and
Board of Directors
South Carolina State Agency of Vocational Rehabilitation
October 18, 2002

We were not engaged to and did not conduct an audit, the objective of which would be the expression of an opinion on the specified areas, accounts, or items. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of the Governor and of the governing body and management of the South Carolina State Agency of Vocational Rehabilitation and is not intended to be and should not be used by anyone other than these specified parties.


for Thomas L. Wagner, Jr., CPA
State Auditor

ACCOUNTANT'S COMMENTS

SECTION A - MATERIAL WEAKNESSES AND/OR VIOLATIONS OF STATE LAWS, RULES OR REGULATIONS

The procedures agreed to by the agency require that we plan and perform the engagement to obtain reasonable assurance about whether noncompliance with the requirements of State Laws, Rules, or Regulations occurred and whether internal accounting controls over certain transactions were adequate. Management of the entity is responsible for establishing and maintaining internal controls. A material weakness is a condition in which the design or operation of one or more of the specific internal control components does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Therefore, the presence of a material weakness or violation will preclude management from asserting that the entity has effective internal controls.

The conditions described in this section have been identified as material weaknesses or violations of State Laws, Rules, or Regulations.

RECONCILIATIONS

Section 2.1.7.20 C. of the Comptroller General's Policies and Procedures (STARS) requires that all agencies perform regular monthly reconciliations of revenues, expenditures, federal programs, and ending cash balances in their accounting records and those in STARS as shown on the Comptroller General's reports in order to timely detect and correct errors. These reconciliations must be performed at least monthly on a timely basis, be documented in writing in an easily understandable format with all supporting workpapers maintained for audit purposes, be signed and dated by the preparer, and be reviewed and approved in writing by an appropriate agency official other than the preparer. Furthermore, STARS states that errors discovered through the reconciliation process must be promptly corrected in the agency's accounting records and/or STARS as appropriate.

For fiscal year 2001 we noted the following deficiencies in reconciliations and reconciliation procedures:

1. The State Agency did not prepare all required reconciliations for each month of fiscal year 2001. Reconciliations of federal programs, which include a reconciliation to the Comptroller General's CSA 467 report and a reconciliation of expenditures, were performed for the months of May, June and fiscal month 13 only. Reconciliations of cash balances were only performed for fiscal month 13.
2. None of the reconciliations were signed and dated by the preparer. There was no evidence that the reconciliations were reviewed.
3. The State Agency did not prepare a reconciliation of revenue by subfund and object code or a reconciliation of expenditures by subfund. Also, no reconciliations were performed for certain of the State Agency's programs.

A similar finding was described in the fiscal year 2000 report. Management stated that it began preparing some of the required reconciliations in response to the prior year audit finding and was aware that it had not prepared all required reconciliations. According to management, the State Agency cannot perform a reconciliation of expenditures by subfund because the State Agency's accounting system cannot generate the report the accounting staff needs to perform the reconciliations. The State Agency's accounting department was told that it would be several years before the necessary report could be generated.

We compared fiscal year 2001 expenditures recorded in STARS to those of the prior year to determine the reasonableness of amounts paid and recorded by expenditure account. Finance personnel were unable to provide adequate explanations for significant expenditure variances in several accounts. Again, this appears to be the result of weaknesses in the State Agency's reconciliation policies and procedures and its financial accounting system.

We recommend that the State Agency develop and implement procedures to ensure that all required reconciliations are prepared and reviewed in accordance with State policy.

CLOSING PACKAGES

Introduction

The Office of the Comptroller General (OCG) obtains certain generally accepted accounting principles (GAAP) data for the State's financial statements from agency-prepared closing packages because the State's accounting system (STARS) is on a budgetary basis. We determined that the State Agency submitted to the OCG certain incorrectly prepared and/or misstated fiscal year-end 2001 closing packages.

To accurately report the State Agency's and the State's assets, liabilities, and current year operations, the GAAP closing packages must be complete and accurate. Furthermore, Section 1.8 of the Comptroller General's GAAP Closing Procedures Manual (GAAP Manual) states, "Each agency's executive director and finance director are responsible for submitting . . . closing package forms . . . that are: •Accurate and completed in accordance with instructions. •Complete. •Timely." Also, Section 1.8 requires an effective, independent supervisory review of each completed closing package and the underlying working papers and accounting records and completion of the reviewer checklist and lists the minimum review steps to be performed. In addition, Section 1.9 directs agencies to keep working papers to support each amount and other information they enter on each closing package form.

The following outlines the errors noted on certain 2001 closing packages.

Miscellaneous Revenues

The State Agency incorrectly reported grant miscellaneous accounts receivable on the miscellaneous accounts receivable and related accounts summary form, resulting in a \$35,399 understatement. State Agency personnel incorrectly calculated the amount of interagency accounts receivable used to determine net accounts receivable reported on the summary form. In addition, gross accounts receivable reported on the June 30, 2001 work centers' consolidated financial statements equaled \$2,260,478; however, gross accounts receivable included in the State Agency's "Workshop Accounts Receivable Report" equaled \$2,255,098, a difference of \$5,380. According to State Agency personnel, the State Agency's Information Systems department had difficulty preparing this report and could not determine why it did not agree to the work centers' financial statements.

Section 3.4 of the GAAP Manual provides guidance for the preparation of the miscellaneous accounts receivable and related accounts summary form. In addition, an effective internal control system requires that adequate supporting documentation be prepared and retained and financial and related information be properly recorded in the accounting and other agency records and be properly summarized in reports prepared therefrom.

Grant/Entitlement Revenues

The State Agency incorrectly reported grant deferred revenue on the grant/entitlement receivables and deferred revenue summary form, resulting in a \$3,932 understatement. Total expenditures for the disability determination grant were incorrectly reported on the grants analysis worksheet that was used to calculate deferred revenue and receivables; therefore, the amount of deferred revenue reported on the summary form was incorrect. We noted that expenditures for this grant were also incorrectly reported on the State Agency's fiscal year 2001 Schedule of Federal Financial Assistance which was used to prepare the grants analysis worksheet.

GAAP Manual Section 3.3 provides guidance for the preparation of the grant/entitlement revenues closing package.

Recommendations

We recommend that the State Agency implement procedures to ensure that all future closing packages contain accurate and complete information in accordance with the GAAP Manual instructions. As required by the GAAP Manual, the State Agency's closing package procedures should include an effective independent review before submitting the forms to the OCG. Each closing package review at a minimum should include the following steps: determine the accuracy and adequacy of documentation prepared, retained and cross-referenced to support each closing package response (monetary and other); determine the reasonableness of each closing package response; agree each response to the closing package worksheets and other supporting documentation and to the accounting and other source records; verify the methodology and formulas used in the supporting documentation and the computations in the working papers and on the closing package; and complete the applicable Closing Package Reviewer Checklist.

TIMING OF DEPOSITS

During our test of cash receipts, we noted 2 out of 25 deposits tested contained receipts which were not deposited timely. In addition, during our cut off test of revenue, we also noted 2 out of 25 deposits contained receipts which were not deposited timely. The State Agency held these funds approximately two weeks to three months from the receipt of the funds until they were deposited. Because cash is the asset which is most vulnerable to loss, adequate internal control procedures require the agency to initiate accounting control over monies immediately upon collection and to timely deposit receipts. Furthermore, Part 1B of each Appropriation Act (Proviso 72.1. of the 2001 Act) requires that all revenues be deposited at

least once each week when practical. Similar findings were reported in the three prior engagements.

We again recommend that the State Agency implement procedures to ensure that all receipts are deposited in a timely manner.

WORKERS' AND UNEMPLOYMENT COMPENSATION INSURANCE

The State Agency paid one hundred percent of workers' and unemployment compensation insurance out of federal funds. Management indicated it was unaware of this problem or that it occurred. A similar finding was described in the fiscal year 2000 report.

Proviso 63G.1. of the fiscal year 2001 Appropriation Act states, "It is the intent of the General Assembly that any agency of the State Government whose operations are covered by funds from other than General Fund Appropriations shall pay from such other sources a proportionate share of the employer costs of retirement, social security, workmen's compensation insurance, unemployment compensation insurance, health and other insurance for active and retired employees, and any other employer contribution provided by the State for the agency's employees."

We recommend the State Agency establish and implement policies and procedures to ensure that workers' and unemployment compensation insurance costs are charged equitably among all of its funds.

SECTION B - STATUS OF PRIOR FINDINGS

During the current engagement, we reviewed the status of corrective action taken on each of the findings reported in the Accountant's Comments section of the State Auditor's Report on the State Agency for the fiscal year ended June 30, 2000, and dated August 14, 2001.

We determined that the State Agency has taken adequate corrective action on the findings entitled Employee Profiles and Journal Vouchers. The continuing deficiencies are described in Reconciliations, Closing Packages, Timing of Deposits and Workers' and Unemployment Compensation Insurance in Section A of the Accountant's Comments in this report.

MANAGEMENT'S RESPONSE

**Agree-upon Procedures Audit
State Fiscal Year 2001**

Response to Accountant's Comments

Reconciliations

1. *The State Agency did not prepare all required reconciliations for each month of fiscal year 2001.* There were a number of staff changes during fiscal year 2001, and we immediately implemented this recommendation from the fiscal year 2000 agreed-upon procedures report we received in April 2001 for the months of May, June and fiscal month 13. We fully implemented this recommendation in fiscal year 2002.
2. *None of the reconciliations were signed and dated by the preparer. There was no evidence that the reconciliations were reviewed.* We implemented this recommendation in fiscal year 2002.
3. *The State Agency did not prepare a reconciliation of revenue by subfund and object code or a reconciliation of expenditures by subfund.* As stated in the finding, our current accounting system does not have the capability of generating revenue reports by subfund and object code or expenditure reports by subfund. Our Information Technology department is unable to provide this information until after our financial system undergoes a process improvement phase. *Also, no reconciliations were performed for certain of the State Agency's programs.* We fully implemented this recommendation in fiscal year 2002.
4. *Finance personnel were unable to provide adequate explanations for significant expenditure variances in several accounts.* Our accounting system does not provide sufficient detail within expenditure accounts to allow complete analysis of expenditure variances. Again, the Information Technology department is unable to provide this information until our system undergoes process improvement.

Closing Packages

1. Miscellaneous Revenues
We concur with the recommendation. We have been working with the Information Technology department on the system issues that led to the understatement of grant miscellaneous accounts receivable as well as the difference between work centers' consolidated financial statements and the "Workshop Accounts Receivable Report". Part of the problem is due to conversion of mainframe data to the PC client network system back in August 2000. Mainframe data was not converted to a relational database, so many of the files are "flat" files meaning they are not integrated within all related programs in the system.
2. Grant/Entitlement Revenues
We concur with the recommendation.

Timing of Deposits

During our test of cash receipts, we noted 2 out of 25 deposits tested contained receipts which were not deposited timely. In addition, during our cut off test of revenue, we noted 2 out of 25 deposits contained receipts which were not deposited timely. One receipt in question was held 11 days until the difference between check amount and invoice amount could be resolved. Another receipt was held 8 days before being deposited. We have implemented procedures to ensure that receipts are deposited at least weekly where practical in compliance with Part 1B of the Appropriation Act (Proviso 72.1 of the 2001 Act).

Workers' and Unemployment Compensation Insurance

The State Agency paid one hundred percent of workers' and unemployment compensation insurance out of federal funds. We concur with this recommendation.

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